Great Canadian Oil Sands Limited

Annual Report 1978

Directors

Theodore A. Burtis, Radnor, Pa.
President and Chief Executive Officer, Sun Company, Inc.

Stanley A. Cowtan, Edmonton
President and Chief Officer of the Company

Kenneth F. Heddon, Toronto
Chairman of the Board of the Company

Ross A. Hennigar, Toronto
President, Sun Oil Company Limited

Gordon E. Hillhouse, Radnor, Pa.
Executive Vice-President, Sun Company, Inc.

F. Newton Hughes, Edmonton
Chairman of the Board, Capwest Capital Services Ltd.

Ardagh S. Kingsmill, Toronto
Partner, Tilley, Carson & Findlay

Robert McClements, Jr., Radnor, Pa.
Executive Vice-President, Sun Company, Inc.

Dudley M. McGeer, Toronto
Vice-President, Administration, Sun Oil Company Limited

William S. McGregor, Edmonton
President, Numac Oil & Gas Ltd.

John E. Poole, Edmonton
Company Director

Bruce W. Watson, Calgary
President, Canadian Homestead Oils Limited

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Chairman of the Board

Ross A. Hennigar
Deputy Chairman of the Board

Stanley A. Cowtan
President and Chief Officer

Joseph S. Camp, Fort McMurray
Vice-President, Operations

William L. Oliver, Edmonton
Vice-President, Corporate Affairs

Dudley M. McGeer
Vice-President, Administration

Ardagh S. Kingsmill
Secretary

Anthony A.L. Wright, Toronto
Treasurer and Assistant Secretary

Joseph E. Wolfe, Edmonton
Assistant Secretary and Assistant Treasurer

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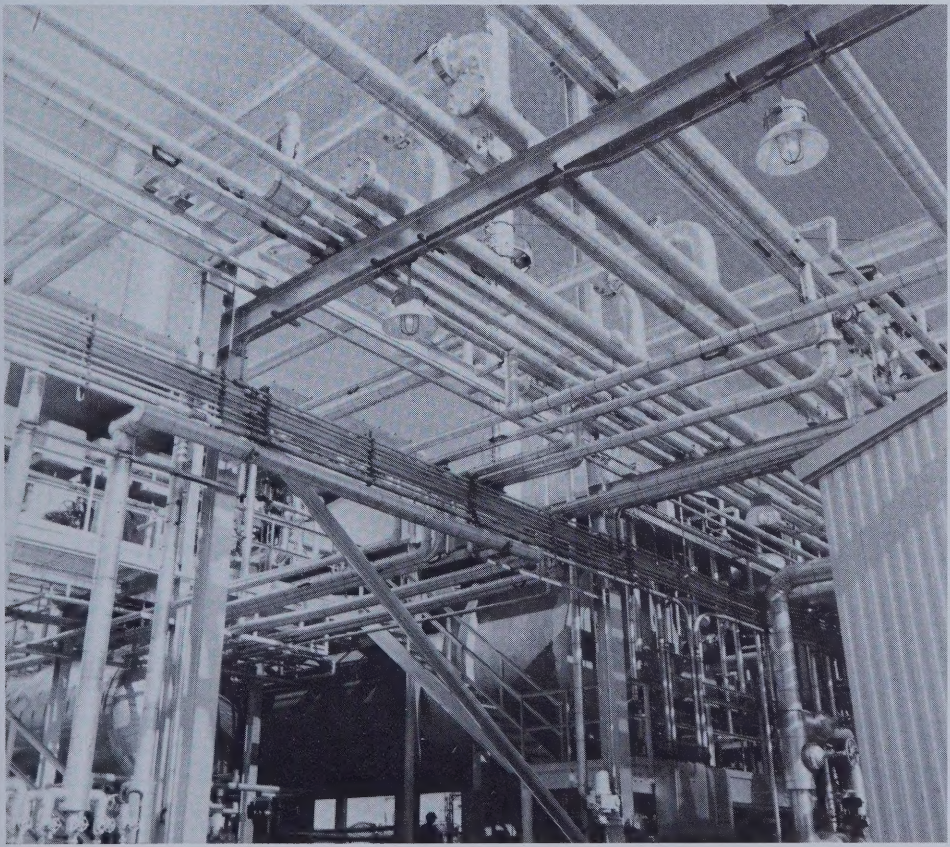
Transfer Agent and Registrar
The Canada Trust Company
110 Yonge Street, Toronto, Ontario
10150 - 100th Street, Edmonton, Alberta
239 - 8th Avenue S.W., Calgary, Alberta

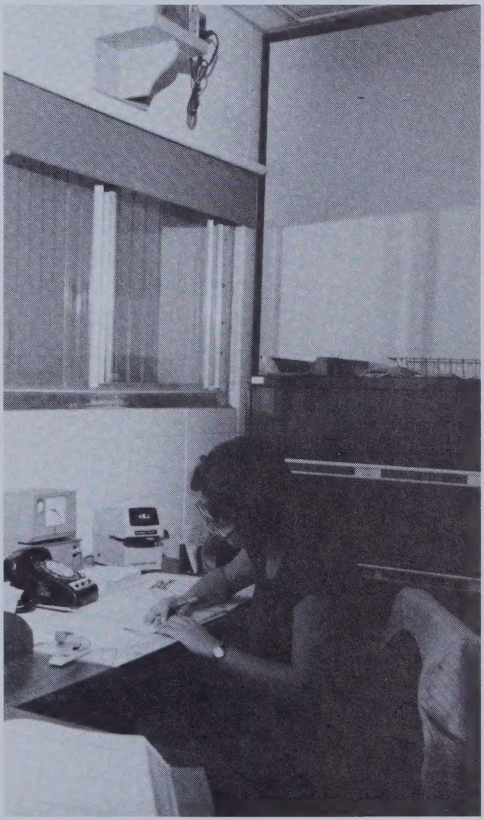
General Counsel
Tilley, Carson & Findlay
Toronto, Ontario

Cover: *A view of the Process coking towers and the Utilities plant.*

Highlights of the Year

	1978	1977	%
Financial	*(Dollars in thousands)*		*Change*
Revenues	$213,186	$180,558	18
Profit before extraordinary gain	19,012	11,385	67
Net profit for the year	19,012	12,917	47
Cash flow from operations	47,351	30,476	55
Capital expenditures	18,498	25,343	(27)
Total assets	379,969	350,696	8
Accumulated deficit	35,310	54,322	
Operating			
Average daily production of synthetic crude (barrels)	44,750	44,914	—
Overburden removed (thousands of cubic yards)	9,668	11,946	(19)
Oil sands mined (thousands of short tons)	33,655	35,295	(5)


A portion of new $7 million sulphur plant commissioned in June, 1978.


Debbie Faucher, Store Person, Materials Management Warehouse, takes orders for parts.

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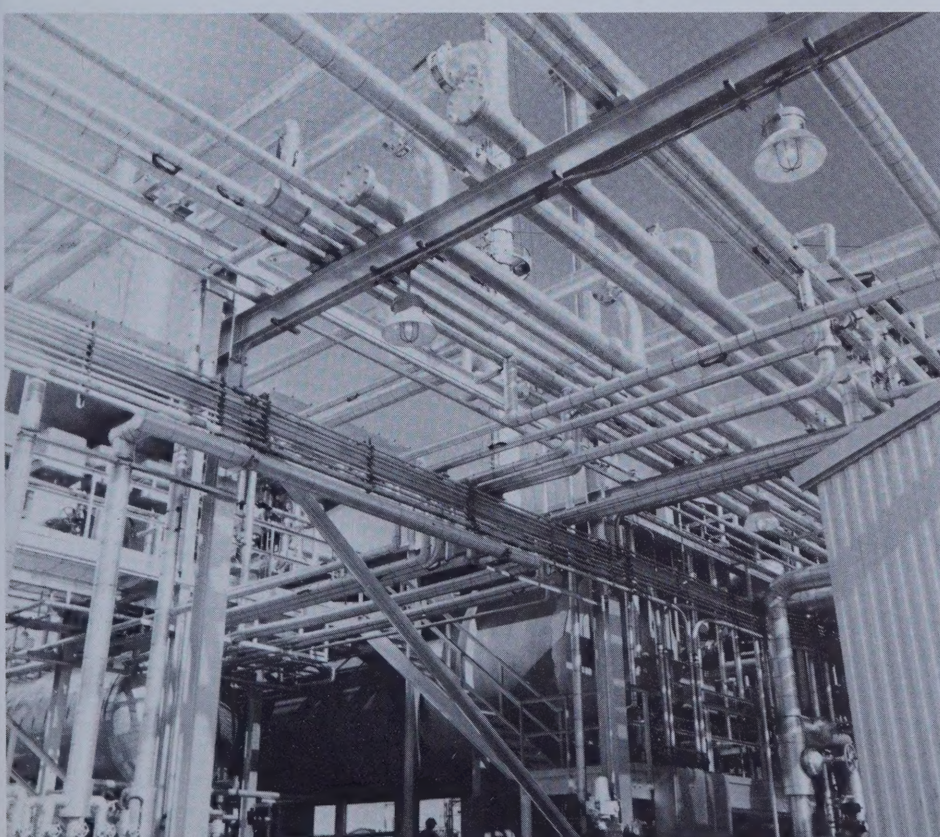
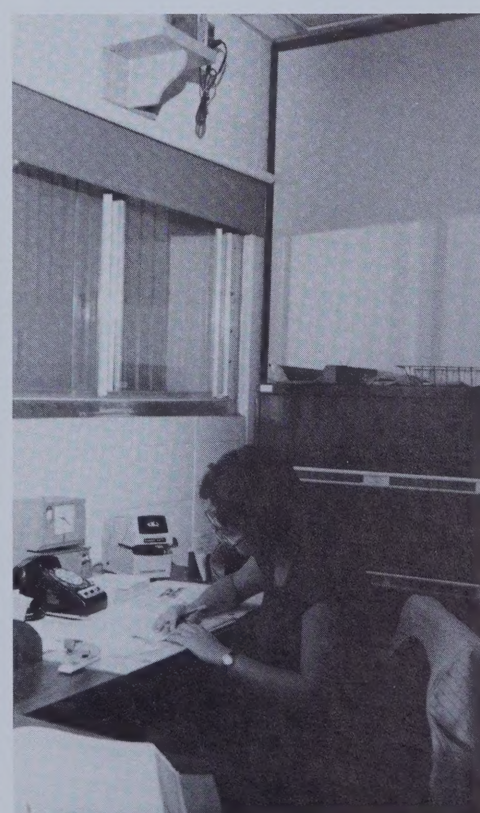
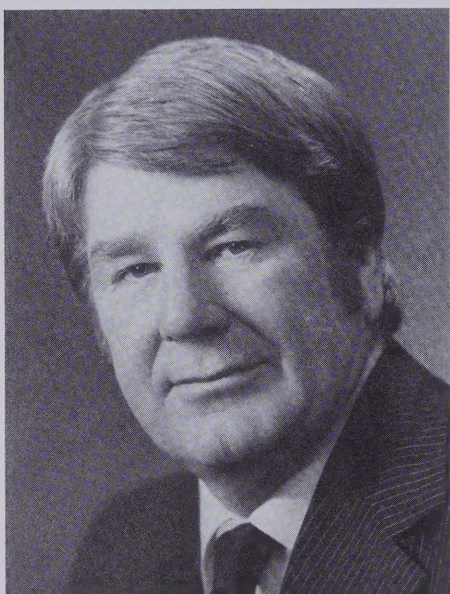


A portion of new $7 million sulphur plant commissioned in June, 1978.



Debbie Faucher, Store Person, Materials Management Warehouse, takes orders for parts.

Report of the President



The year 1978 was a mixed one for our company. While production of synthetic crude fell slightly compared to the previous year, earnings increased. At the same time, two announcements were made concerning events which could have a significant effect on the company's future.

At a daily average of 44,750 barrels, output of synthetic crude was just under that reported for 1977. Production failed to exceed 1977 levels for two reasons. One was the 39-day strike by members of the union representing the company's operating employees. The second centred on mechanical difficulties which occurred in some of the process units early in the year and also during the last quarter.

Earnings, though affected by the lower-than-expected production, increased to $19 million, compared to the $12.9 million reported for 1977. The improvement resulted largely from two $1.00 increases in the price per barrel of crude oil by the Federal Government which went into effect on January 1 and July 1, respectively. Revenues for the year rose to $213 million. At the same time, our cash flow from operations increased to $47 million, up $17 million over 1977. The company's improved financial position is reflected in our higher working capital which was up by about $28 million. Despite a significant improvement in managing direct controllable plant costs, overall there was a sharp increase in expenses during 1978. A major portion of the increase reflects a modification in the application of our capitalization policy which was announced during the first quarter of 1978 and became effective January 1, 1978. Additional information on this policy is in the notes to the financial statements.

The two announcements, made in the latter half of 1978, concerned the proposed amalgamation with Sun Oil Company Limited and the plan to expand the plant.

The announcement of the proposed amalgamation with Sun Oil Company Limited, a sister Canadian company, was made last September. A Management Proxy Circular will give you full particulars of the proposal. We hope each of you will read the circular carefully prior to the shareholders' meeting at which you will be asked to approve the amalgamation.

The expansion would add about 13,000 barrels daily to production capacity at an estimated cost of $185 million. Construction is planned to begin in 1979 and is expected to be substantially completed in 1981. Fully expanded production is expected to be reached in 1982. With the decision to expand and in keeping with the Federal Government policy to encourage development of non-conventional petroleum sources, GCOS will begin receiving world prices for its crude effective upon approval by the Alberta Government. Company management is optimistic that timely approval will be obtained. Alberta, also supportive of additional oil sands production, will levy an average monthly royalty rate similar to the present one on the additional production.

A regrettable development in 1978 and one of concern to the management of the company was the 39-day strike which occurred in September and October. The primary issue, which difficult and protracted pre-strike negotiations failed to settle, involved extensive overtime worked by mobile equipment maintenance personnel. We wanted to establish hours of work for these employees which were consistent with the practice in other areas of the plant. The final settlement corrected this anomaly and should help us to improve the efficiency and the effectiveness of this labour-intensive portion of our business.

The strike, unwelcome as it was, created some opportunities. About three weeks after the strike began, supervisory and professional personnel started-up the plant, initially operating it at reduced volumes and achieving an average daily production of 45,000 barrels per day during the latter part of the strike. As a result of their commitment and hard work, the net effect of the 39-day strike was 27 days of lost

production. For the non-operating staff, it meant added experience through hands-on operating exposure. As well, the work stoppage allowed the company to re-assess plant staffing and it is likely that we will be able to operate existing facilities with fewer people. Any reduction in staff would be achieved through attrition.

The key objective of GCOS in the coming year will continue to be the production of synthetic crude oil at the maximum stable rate consistent with good operating practices and recovery economics. An important parallel activity will be a continuing stringent control of expenses. To help achieve this latter objective, a special study is underway to further improve the effectiveness of our cost control measures in all areas of the plant.

The company's financial performance remains far from satisfactory. The deficit, which has been slowly reduced, stood at about $35 million at the end of 1978. Lease royalties payable to Sun Oil Company Limited continue to be waived. If these royalties had been paid, they would have amounted to almost $22 million in 1978 with an accumulated total of $95 million since the waiver went into effect. Neither has the company been in a position to pay the seven per cent annual dividend on the $165 million in preferred shares nor have any dividends been paid on the common shares.

During 1979, the company plans to spend some $26 million on improving its production facilities, on environmental protection equipment, and on new employee housing. The major portion, about $18 million, is for work on a $22 million electrostatic precipitator for the powerhouse stack. The precipitator is a significant environmental protection measure which will reduce particulate emissions. These funds do not include those capital expenditures, about $19 million, earmarked for expansion in 1979.

The coming spring will see a planned production halt for the biennial maintenance shutdown. Intense planning has been underway since the last shutdown as both necessary maintenance work and certain preparations for the expansion project will be undertaken simultaneously.

On the following pages, shareholders will find more detailed operational reports on the plant. We hope that each of you will take the time to read these reports along with the financial statements. Your interest in the company is both welcomed and encouraged.

S. A. Cowtan

S. A. Cowtan
January 24, 1979

Operations

Operating Report

During 1978, Great Canadian Oil Sands Limited produced for shipment 16,334,000 barrels of synthetic crude, an average daily output of 44,750 barrels. This is about the same level of production as in 1977 when we underwent a planned maintenance shutdown. The lack of production improvement was caused by a strike of the company's operating personnel as well as problems in the process units early in the year and during the last quarter. The following is a report on the key segments of the plant's operations.

Mine

Overburden removed during the year totalled 9.7 million cubic yards. This was a sharp drop from 1977 and was caused by difficulties with overburden removal equipment, stretches of unseasonably wet weather and the employee strike. To avoid hampering this winter's mining operations, outside contractors were hired to strip overburden from a supplemental mining area.

The quantity of oil sands mined remained close to last year's levels. Together the primary and supplementary mining systems excavated some 33.7 million tons of ore. Mining of Lease 86 is now proceeding in a northerly direction, completing the move begun in 1977 when the mine reached the western boundary of the lease.

A new extension to the main feed conveyor system was constructed in 1978. The extension services a supplemental mining area on the eastern section of the lease and later will serve the future main mining area as it is opened up.

A further core hole drilling program was begun in 1978. By completion in 1979, some additional 400 holes will have been drilled on the lease site. The additional knowledge of the ore body will assist in planning and implementing future mining operations.

Extraction

The extraction plant operated satisfactorily in 1978. A number of improvements were made to the plant's facilities during the year. Among these were modifications to the bins which accept the ore from the mine conveyor system. These modifications enable a more uniform rate of flow of oil sand to the conditioning drums. Improved design of the conditioning drums was another step taken to better efficiency. Working conditions within the plant also have been upgraded through additional heating-ventilating equipment.

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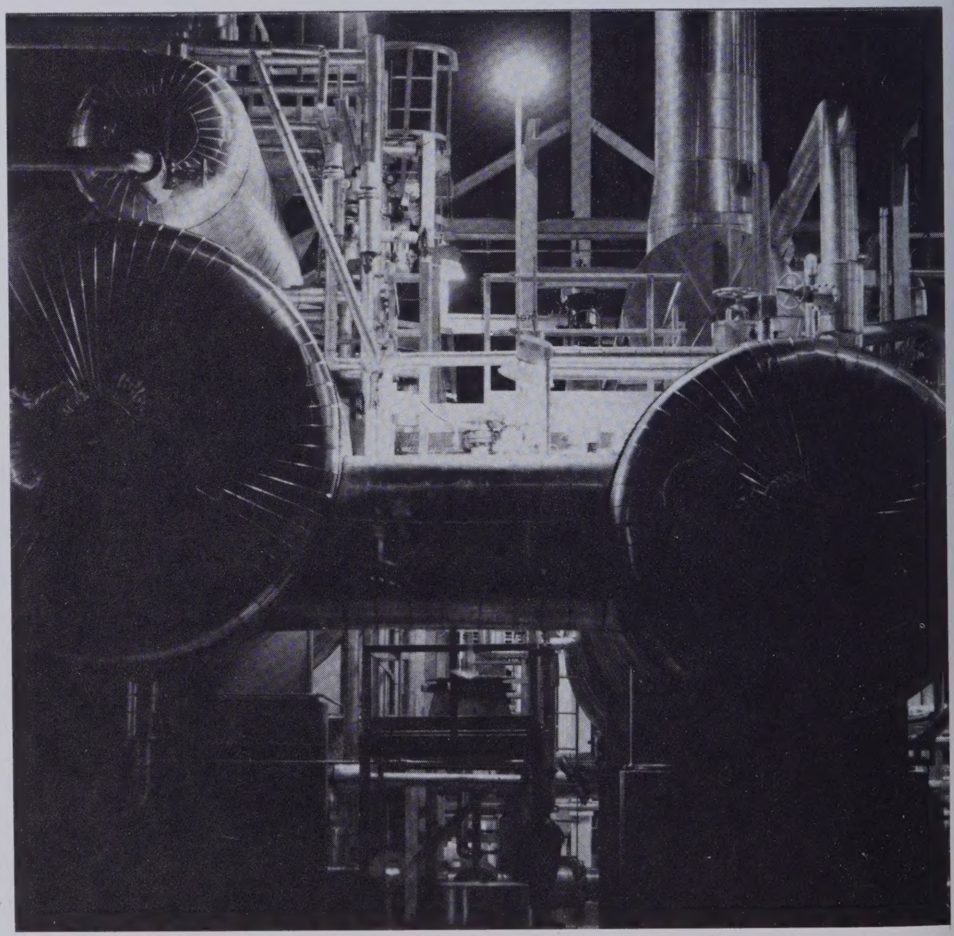
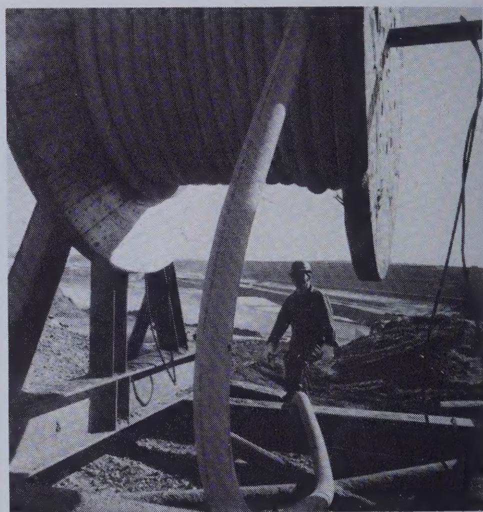


A night view of the new sulphur plant.


Location
Map
Future
mining
area
Lean
sands
area
Plant
area
Worked-out pit
Tailings
pond
GCOS lease boundary
Athabasca River
FORT
McMURRAY
Peace River
GCOS
Pipeline
Athabasca River
EDMONTON
ALBERTA
CALGARY

1 *Roger Deblois cutting pipe to standard lengths for use in dyke construction.*
2 *Maintenance crew working on the rotary plate of bucketwheel excavator 1301.*
3 *Trailing cable is laid to tailings pond pump.*
4 *Frank Simon, Catalytic Machinist, mills a sight glass for pipefitters.*
5 *Bottom bench conveyor carries oil sand through culvert to the extraction plant.*

1



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Great Canadian Oil Sands Limited

Financial Statements
1978

Statement of Performance *for the year ended December 31*

Great Canadian Oil Sands Limited and Subsidiaries

	1978	1977
	Thousands of dollars	
Revenues		
Sales and other operating	$210,139	$178,685
Interest	3,047	1,873
	213,186	180,558
Expenses		
Overburden removal (note 5)	18,267	12,225
Plant operations	96,905	89,226
Depreciation (note 5)	10,742	9,966
Amortization of deferred preproduction costs	1,967	1,900
Crown royalty	26,051	21,846
Lease royalty (notes 13 and 15)	9,075	7,614
Administrative and general	12,462	10,944
Interest (note 6)	5,110	5,456
Income taxes (note 7)	13,595	9,996
	194,174	169,173
Profit before extraordinary gain	19,012	11,385
Extraordinary gain (note 8)	—	1,532
Net profit	$ 19,012	$ 12,917

See accompanying notes

Auditors' Report

To the Shareholders of
Great Canadian Oil Sands Limited

We have examined the consolidated statement of financial position of Great Canadian Oil Sands Limited as at December 31, 1978 and the consolidated statements of performance and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1978 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles which, except for the changes described in Note 2 to the financial statements, have been applied on a basis consistent with that of the preceding year.

COOPERS & LYBRAND
Chartered Accountants
Edmonton, Canada
January 24, 1979

Statement of Financial Position *as at December 31*

Great Canadian Oil Sands Limited and Subsidiaries

	1978	1977
	(Thousands of dollars)	
Cash and items convertible to cash within one year		
Cash	$ —	$ 486
Short-term investments	16,996	—
Amounts due from: customers	7,550	15,648
affiliated companies	11,894	—
others	3,329	2,813
Inventories: product	6,665	4,661
materials and supplies	15,921	15,586
	62,355	39,194
Deduct: Liabilities payable within one year		
Short-term borrowings	3,741	11,100
Amounts due to: suppliers and others	27,759	23,928
affiliated companies	—	1,045
Taxes other than income taxes	1	359
Current portion of long-term borrowings	2,745	2,519
	34,246	38,951
Working capital	28,109	243
Add: Other assets		
Properties, plant and equipment (note 9)	197,516	194,754
Housing (note 9)	37,854	36,962
Deferred foreign exchange loss (note 2)	3,105	—
Expenditures for the benefit of future years:		
Deferred preproduction costs	49,981	50,146
Deferred overburden removal costs (note 5)	29,158	29,640
	317,614	311,502
Working capital plus other assets	345,723	311,745
Deduct:		
Long-term borrowings:		
Notes (note 10)	37,936	36,563
Mortgages on housing (note 11)	24,576	24,578
Deferred income taxes	27,289	13,694
	89,801	74,835
Shareholders' equity	$255,922	$236,910
Shareholders' equity consists of:		
Preferred shares (note 12)	$165,000	$165,000
Common shares (note 12)	126,232	126,232
	291,232	291,232
Deficit		
Beginning of year	(54,322)	(67,239)
Net profit for the year	19,012	12,917
End of year	(35,310)	(54,322)
	$255,922	$236,910

On behalf of the Board
S.A. Cowtan, Director
D.M. McGeer, Director

See accompanying notes

Statement of Changes in Financial Position *for the year ended December 31*

Great Canadian Oil Sands Limited and Subsidiaries

	1978	1977
	(Thousands of dollars)	
Source of working capital		
Profit before extraordinary gain	$19,012	$11,385
Add back (deduct) items not affecting working capital:		
Depreciation (note 5)	10,742	9,966
Amortization of deferred foreign exchange loss	639	—
Amortization of deferred preproduction costs	1,967	1,900
Deferred overburden removal costs (note 5)	2,064	(2,487)
Gain on disposals of properties, plant, equipment and housing	(668)	(284)
Deferred income taxes	13,595	9,996
	47,351	30,476
Disposals of properties, plant, equipment and housing	3,188	3,770
New mortgages payable on housing	1,797	5,276
Additions to working capital	52,336	39,522
Use of working capital		
Purchases of properties, plant and equipment	14,644	19,035
Housing	3,854	6,308
Preproduction costs (note 13)	1,802	—
Borrowings maturing within one year	4,170	2,845
Reductions in working capital	24,470	28,188
Net increase in working capital	27,866	11,334
Working capital (deficiency) — beginning of year	243	(11,091)
Working capital — end of year	$28,109	$ 243
Analysis of the change in working capital		
Cash	$ (486)	$ 394
Short-term investments	16,996	—
Amounts due from customers, affiliated companies and others	4,312	2,404
Inventories	2,339	3,536
Short-term borrowings	7,359	9,333
Amounts due to suppliers, affiliated companies and others	(2,786)	(4,557)
Taxes other than income taxes	358	192
Current portion of long-term borrowings	(226)	32
Net increase in working capital	$27,866	$11,334

See accompanying notes

Notes to Consolidated Financial Statements *December 31, 1978*

Great Canadian Oil Sands Limited and Subsidiaries

1. Summary of significant accounting policies

a) Consolidation —
The accompanying financial statements are prepared on a consolidated basis to include the accounts of all subsidiaries.

b) Inventories —
Inventories are valued at the lower of average cost and estimated net realizable value.

c) Depreciation and amortization —
Properties, plant and equipment capitalized after January 1, 1976 are depreciated over the lesser of their useful lives or the life of estimated reserves except that the cost of equipment relating to the mining operation is, with specific exceptions, expensed as incurred. All production facilities capitalized prior to January 1, 1976 are depreciated on the basis of estimated reserves. Effective January 1, 1978, only major additions and improvements to the productivity or environmental protection systems of the plant are capitalized.

Rental housing, mobile equipment and furniture and fixtures are depreciated over their estimated useful lives.

Depreciation over useful lives is charged to expense on a straight line basis. The write-off periods of the significant depreciable assets range from 5 to approximately 23 years.

Deferred preproduction costs are amortized on the basis of estimated reserves. Overburden removal costs are amortized on the basis of the ratio of total overburden to oil sands reserves. Deferred overburden removal costs will increase or decrease when the ratio of overburden removed to oil sands mined, in the current year, exceeds or is less than the forecast average ratio.

d) Maintenance, repairs and shutdown expenses —
Normal maintenance and repairs are charged to expense as incurred. The cost of major maintenance shutdowns is estimated and accrued over the period between each shutdown.

e) Income taxes —
Some costs and revenues may by law be deducted or added in calculating taxable income in years later or earlier than actually recorded in the financial statements. The income taxes in the Statement of Performance are based upon the revenues and expenses actually recorded, but differ from taxes actually paid or payable, if any. These differences are shown in the Statement of Financial Position as deferred income taxes.

f) Pension expense —
The Company has a contributory pension plan providing retirement benefits for its employees. Pension expense includes the amortization of initial past service costs over 25 years and the amortization of plan improvements over 15 years. It is the Company's policy to fund the total pension expense.

2. Change in accounting policy, and in the application of accounting policy

a) Foreign currency translation —
In 1978, as recommended by the Canadian Institute of Chartered Accountants, the Company adopted the temporal method of accounting for the translation of foreign currencies. As the method presently relates to the Company, liabilities payable in foreign currencies are translated to Canadian dollars at the year-end exchange rate, and unrealized exchange gains and losses are amortized over the repayment period. This change in method has not been applied retroactively. In prior years translation of non-current amounts into Canadian dollars was at the exchange rate on the transaction date. Amounts transferred from long-term borrowings to liabilities payable within one year were adjusted at the current exchange rate.

At December 31, 1978 an unrealized exchange loss of $3,105,000 has been deferred. As a result of the change, administrative and general expenses for the year are increased, and net profit is reduced, by $419,000. If this recommendation had been retroactively applied, the deficit as at December 31, 1977 would have been increased by $111,000.

b) Capitalization of properties, plant and equipment —
Effective January 1, 1978, the Company modified the application of its fixed asset capitalization policy as it relates to the plant, such that only major additions and improvements to productivity or environmental protection systems are capitalized. For 1978 this modification resulted in an increase in expenses before income taxes of $9,790,000 and a net profit decrease of $6,933,000.

3. Changes in statement presentation

1977 figures have been reclassified on a basis consistent with 1978.

4. Estimated reserves

For the purpose of determining the amounts of certain depreciation and amortization in the accounts, the remaining reserves of synthetic crude oil at December 31, 1978 have been estimated at approximately 420 million barrels. The actual quantity capable of economic recovery will depend in part upon the future relationship between synthetic crude selling prices and costs.

5. Deferred overburden removal costs

	1978	1977
Outlays during the year	$16,203,000	$14,712,000
Overburden removal expensed	18,267,000	12,225,000
	(2,064,000)	2,487,000
Depreciation on equipment for the year	1,582,000	1,805,000
Balance — beginning of year	29,640,000	25,348,000
Balance — end of year	$29,158,000	$29,640,000

The above depreciation on overburden removal equipment is not included in depreciation expense of $10,742,000 (1977 — $9,966,000).

6. Interest expense

	1978	1977
Short-term	$ 400,000	$1,264,000
Notes and mortgages	4,710,000	4,192,000
	$5,110,000	$5,456,000

7. Income taxes

The Company accounts for income taxes as set out in Note 1. The income tax provision in the Statement of Performance reflects a different amount from that which would arise from application of the statutory tax rate. A reconciliation of the Statement and statutory tax rates is as follows:

	1978	1977
Statutory rate	47.0%	47.0%
Crown royalty disallowance	37.6	48.0
Other permanent disallowance	1.4	0.9
Resource allowance	(24.0)	(27.0)
Depletion allowance	(15.5)	(17.2)
Alberta tax rebate	(4.8)	(4.9)
Provision for income taxes	41.7%	46.8%

8. Extraordinary gain

The 1977 extraordinary gain is the reduction of income taxes resulting from the application of $1,532,000 in Alberta income tax rebates brought forward from prior years. Such rebates may be credited only against Alberta income taxes otherwise payable. Rebates in the amount of $507,000 were exhausted in 1978 and are applied as a reduction of income tax expense in that year.

9. Properties, plant and equipment, and housing

a) Properties, plant and equipment —

These are at cost less accumulated depreciation of $82,260,000 in 1978 and $71,837,000 in 1977.

b) Housing —	1978	1977
Lots, rental housing and housing under construction, at cost, less accumulated depreciation of $1,184,000 in 1978 and $1,798,000 in 1977	**$17,673,000**	$19,487,000
Agreements for sale receivable, at the lower of cost or selling price of houses sold, less principal payments received to date and less principal due within one year	**20,181,000**	17,475,000
	$37,854,000	$36,962,000

10. Notes

These are 5¾% notes in U.S. currency maturing July 1, 1991 repayable $2,000,000 in U.S. currency annually. The total principal amount outstanding at Dec. 31, 1978 is U.S. $34,000,000 of which U.S. $32,000,000 is payable beyond one year.

The method of translating the notes into Canadian currency is described in Note 2.

11. Mortgages on housing

These are repayable over the next 30 years, bearing interest at rates ranging from 6¼ to 11¾ per cent. The estimated principal repayments required on the non-current portion of mortgages payable at December 31, 1978 are as follows:

1980	$ 396,000
1981	412,000
1982	426,000
1983	444,000
Subsequent	22,898,000
	$24,576,000

12. Preferred and common shares

There have been no changes in paid-in capital during the year. The common shares are of no par value and the issued preferred shares are 7% non-cumulative redeemable (at par) voting shares having a par value of $100 each.

	Authorized Shares	Issued Shares
Preferred:		
First	500,000	500,000
Second	500,000	500,000
Third	450,000	450,000
Fourth	550,000	200,000
Total	2,000,000	1,650,000
Common	35,000,000	28,504,259

All the preferred shares and approximately 96.1% of the common shares are owned by Sun Company, Inc.

13. Commitments and contingencies

a) The Company is a party to an agreement with Sun Oil Company Limited and Norcen International Ltd. (formerly CIGOL International Ltd.) involving the sublease of Bituminous Sands Lease No. 86 in respect of which the Company is operating its plant. Lease No. 86 runs for a term of 21 years from June 1, 1966 renewable for further terms each of 21 years subject to such terms and conditions as may be prescribed. The Company is obligated under the provisions of the agreement to pay Sun and Norcen a basic royalty of 10 cents per barrel of bitumen extracted or recovered from bituminous sands from the leased land together with an additional royalty of 25% of synthetic crude revenues in excess of $2.75 per barrel (declining to $2.60 in the future under certain conditions) and subject to a 50% increase in both royalties after the Company's cash flow has equalled its total initial investment. Such royalties are payable 75% to Sun and 25% to Norcen (see Note 15 re waiver by Sun).

The Company is also a party to an agreement with Chevron Canada Limited involving Bituminous Sands Lease No. 23A on which the Company completed mining in 1978.

Under the provisions of this agreement Chevron was paid a gross overriding royalty of 3% of the amount received by the Company for synthetic crude oil sold, attributable to bituminous sands from the lease.

b) Under the provisions of the sale agreements covering the sale of housing units to employees the Company has undertaken, in the event of an employee termination within up to eight years of the date of the sale agreement, to repurchase the employee's housing unit. The potential net outlay under such repurchase commitments is the principal amount paid by the employee to the date of termination plus a portion of any increase in replacement costs between the effective dates of sale and repurchase. The aggregate of such principal amounts paid by employees to December 31, 1978 approximates $3,100,000 but any additional potential outlay resulting from increases in replacement costs cannot be determined until an employee actually terminates employment.

c) The Company is a party to long-term agreements with Sun Oil Company Limited and with Shell Canada Limited pertaining to the sale of synthetic crude oil.

d) An indebtedness to the Government of Canada of $1,802,107 in respect of certain wartime expenditures in the Athabasca oil sands area has been recognized in 1978, has been included in deferred preproduction costs and will be amortized with the balance of such costs.

14. Directors and officers

Twelve persons were directors of the Company during 1978, only certain of whom were paid as such, and their remuneration aggregated $41,500. The nine officers of the Company during 1978 included five who were also directors, their remuneration as officers aggregated $573,800.

15. Sun Oil Company Limited lease royalty waiver

Sun Oil Company Limited has waived, effective April 1, 1970, the royalties to which it is entitled under the agreement described in Note 13 until the elimination of the Company's deficit account or a determination that the financial results from the Company's operations are satisfactory. The reduction in costs due to this temporary relief is as follows:

	1978	1977
Royalties waived for the year	**$21,996,000**	$13,071,000
Cumulative royalties waived	**$95,309,000**	$73,313,000

16. Preferred share dividends and earnings per share

No dividends have been declared or paid to date on the $165,000,000 of 7% non-cumulative preferred shares. Were a deduction made for a full annual dividend of $11,550,000 on the outstanding preferred shares, the earnings per common share would be as follows:

	1978	1977
Profit (loss) per share before extraordinary gain	**$0.26**	$(0.01)
Net profit per share	**$0.26**	$ 0.05

Basic earnings per common share, which are computed without deduction for preferred share dividends (since none have been declared), are as follows: Profit per share before extraordinary gain: **1978 — $0.67** (1977 — $0.40). Net profit per share: **1978 — $0.67** (1977 — $0.46).

17. Plant expansion

The Company has approved an expansion at an estimated cost of $185 million to add about 13,000 barrels of daily production capacity to the plant.

The project is subject to approval by the Alberta Government. In keeping with government policy to encourage energy resource development, the Company has been assured by the Government of Canada that upon Alberta approval the Company will begin to receive world prices for its production. As well, the Alberta Government has indicated that the Alberta crown royalty rate on the expanded production will approximate the present average rate.

The expansion outlays are expected to take place in stages over the next three years.

18. Proposed amalgamation with Sun Oil Company Limited

An amalgamation of Great Canadian Oil Sands Limited with Sun Oil Company Limited has been proposed.

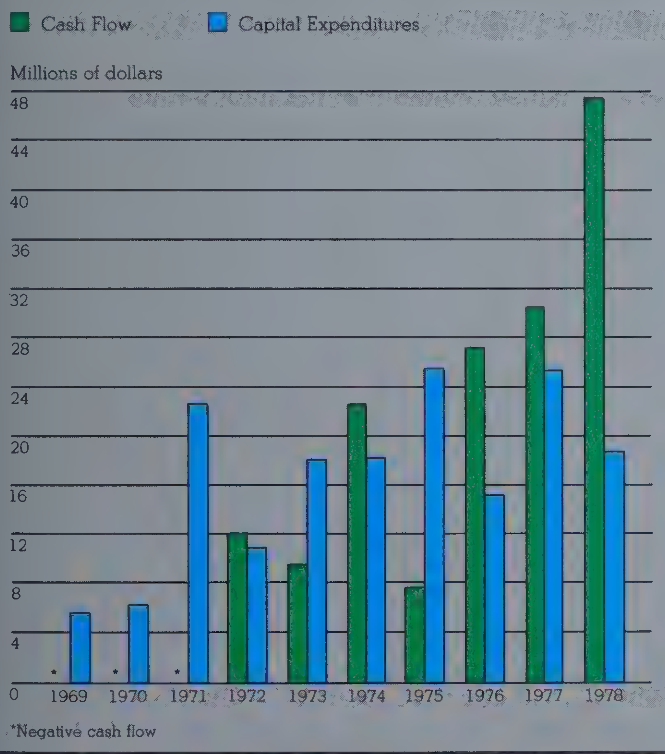
Financial and Operating Ten Year Summary*

	1978	1977	1976	1975	1974	1973	1972	1971	1970	1969
					(Dollars in Millions)					
Financial										
Revenues										
Sales and other operating	**210.2**	178.7	158.3	122.9	106.9	72.1	61.5	50.9	34.8	29.0
Interest	**3.0**	1.9	1.5	1.5	1.2	1.1	1.0	0.7	0.5	0.5
	213.2	180.6	159.8	124.4	108.1	73.2	62.5	51.6	35.3	29.5
Expenses										
Overburden removal	**18.2**	12.2	14.0	9.1	7.3	8.9	9.8	6.3	2.8	2.4
Plant operations	**96.9**	89.2	73.2	69.2	50.1	37.4	31.2	35.1	29.4	28.7
Depreciation	**10.7**	10.0	10.8	8.8	7.8	7.9	7.9	6.5	4.9	4.2
Amortization of deferred pre-production costs	**2.0**	1.9	2.0	1.8	2.0	2.2	2.3	1.9	1.5	1.3
Crown royalty	**26.1**	21.9	19.5	14.8	12.8	8.1	3.7	1.9	1.4	2.0
Lease royalty	**9.1**	7.6	6.8	5.5	4.4	1.7	0.6	0.6	0.4	1.5
Administrative and general	**12.5**	10.9	9.4	9.4	6.2	4.5	3.7	3.4	2.9	3.1
Interest	**5.1**	5.5	6.9	6.8	5.5	4.8	4.0	4.1	8.0	11.8
Income taxes	**13.6**	10.0	8.2	2.7	4.9	—	—	—	—	—
	194.2	169.2	150.8	128.1	101.0	75.5	63.2	59.8	51.3	55.0
Profit (loss) before extraordinary gains	**19.0**	11.4	9.0	(3.7)	7.1	(2.3)	(0.7)	(8.2)	(16.0)	(25.5)
Extraordinary gains	—	1.5	3.0	2.7	4.9	—	—	—	—	—
Net profit (loss)	**19.0**	12.9	12.0	(1.0)	12.0	(2.3)	(0.7)	(8.2)	(16.0)	(25.5)
Items not affecting working capital	**28.4**	17.6	15.2	8.7	10.3	11.8	12.7	6.2	5.3	3.2
Cash flow from operations	**47.4**	30.5	27.2	7.7	22.3	9.5	12.0	(2.0)	(10.7)	(22.3)
Shareholders' equity:										
Preferred and common shares	**291.2**	291.2	291.2	291.2	291.2	291.2	291.2	291.2	276.5	171.1
Deficit	**(35.3)**	(54.3)	(67.2)	(79.2)	(78.2)	(90.2)	(87.9)	(87.2)	(79.0)	(63.0)
	255.9	236.9	224.0	212.0	213.0	201.0	203.3	204.0	197.5	108.1
Capital expenditures	**18.5**	25.3	15.1	25.5	18.3	18.1	10.9	23.0	6.0	5.6
Salaries, wages and benefits**	**43.9**	42.6	35.8	31 3	23.1	14.7	12.2	9.8	7.7	6.1
Operating										
Overburden removal (millions of cubic yards)	**9.7**	11.9	12.1	10.1	10.0	10.1	13.1	9.3	6.8	6.4
Oil sands mined (millions of short tons)	**33.7**	35.3	36.1	32.7	34.5	36.1	39.2	33.2	30.2	26.2
Synthetic crude sold (millions of barrels)	**16.4**	16.4	17.5	15.7	16.5	18.4	18.4	15.5	11.9	10.0

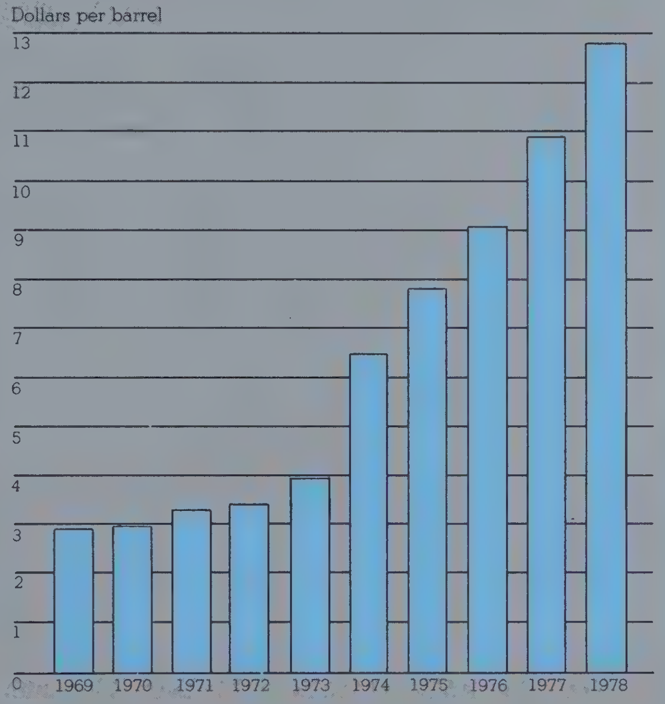
* *Prior years' figures are presented on a basis consistent with 1978 except for changes in accounting policy not applied retroactively (see Notes to Consolidated Financial Statements, notes 1 and 2)*

***In addition, substantial employment is provided at the plant by companies supplying contracted services to Great Canadian Oil Sands Limited*

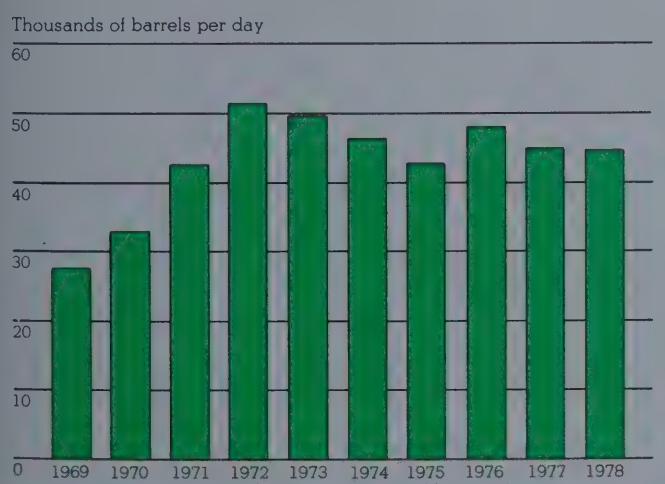
Cash Flow from Operations vs. Capital Expenditures



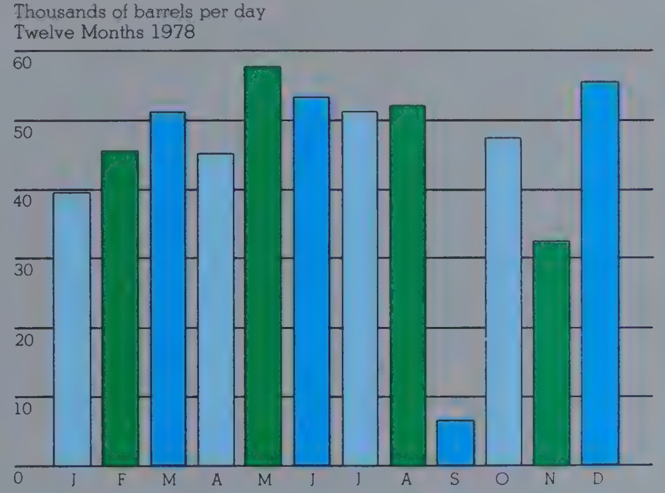
Average Selling Price per Barrel of Synthetic Crude



Synthetic Crude Production



Synthetic Crude Production



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Process

The process facilities experienced operating problems during the year which affected production levels. In the first quarter there were difficulties with the coking units. During the last quarter there were malfunctions with the equipment used to upgrade synthetic crude. The net result was substantially limited production especially in November when average daily output fell to 32,300 barrels.

The new $7 million sulphur plant and amine unit was completed and brought on stream about mid-year. These facilities essentially duplicate the main sulphur plant already in place. They help to strengthen the operation's environmental protection capabilities and maintain synthetic crude production should operating difficulties force the shutdown of the original sulphur plant.

Environmental Protection

The past year saw the company continue the various projects related to its environmental protection program. One such project is tree planting on dyke walls. However, there is difficulty with rodent damage to the younger trees. One way to reduce such damage is to encourage natural predators to the area. For example, the company is trying to attract hawks to the lease by installing nesting boxes and perches.

In a move to further strengthen the environmental protection program, the company expanded the Environmental Affairs Department in 1977. During its first full year of operation in 1978, the department

Lawrence Miller, Utilities Operations, checks plant 35 boiler controls.

Terrylynn Winnington, Equipment Operator, at the wheel of a 150-ton capacity truck.

Maintenance mechanic repairs engine of 150-ton Wabco truck

1 Overburden is loaded into 150-ton trucks by bucketwheel excavator.
2 Slowly rotating drums extract bitumen from oil sands in extraction plant.
3 Main conveyor belt whisks oil sand into extraction plant.

Frank Toner, Mine Operations, cleans bucketwheel excavator 1340, using a high pressure air hose.

conducted a more detailed monitoring of company activities to assess their possible impact on the environment.

During 1978, engineering continued and construction began on a project to reduce particulate emissions to the atmosphere from the powerhouse stack. The project will use electrostatic precipitators to remove the ash from the stack gases. Estimated cost is $22 million and construction is projected for completion in late 1979. This substantial investment in environmental protection will not increase production but will add to the plant's operating expenses.

Our plan for the development and reclamation of the lease up to the end of the lease life was submitted to the Alberta Government in 1978. As required by the Land Surface Reclamation Act, the plan details how mined-out areas would be backfilled and revegetated. Following the submission, several meetings were held with the provincial government and final approval of our plan is anticipated.

Human Resources

The Human Resources function was strengthened in 1978 with the hiring of additional professional personnel. The employee relations function at the plant site was improved in order to continue to develop a more effective union-management relationship.

A formal training program for employees was continued with 10 subjects offered on a scheduled basis. Among the subjects offered in the program are Supervision, Time and Meeting Management, Effective Writing and Counselling. Special training programs also are held as required.

New camp facilities for 500 persons will be completed in early 1979 at a cost of $1.8 million. With the new facilities, the plant site camp will have an 1160-person capacity, enabling it to meet peak work-force requirements such as will be experienced during the 1979 planned maintenance shutdown and the proposed expansion project.

Corporate and Public Affairs

The company continued its program of strengthening its lines of communications with the Government of Alberta and the Federal Government. Close contact was maintained with various government departments at both levels and discussions were held on such subjects as environmental protection, plant expansion, and labour relations.

GCOS also stepped up its communications programs with its various constituents. Two audiences receiving special emphasis are employees and the media. A media relations function was established within the Public Affairs department in 1978 with the primary objective of strengthening the company's contacts among members of the media, particularly in Alberta. It will, for example, encourage media representatives to contact the company for comment on events which can affect the public's perception of GCOS and its operations.

Committees of the Board of Directors

There are three committees of the GCOS Board of Directors: Audit; Manpower and Board Policy; and Public Affairs Policy. The Audit Committee is composed only of directors, the majority of whom are not officers of the company. The Manpower and Board Policy Committee and the Public Affairs Policy Committee have, in addition to directors, members who are not directors, but who have a particular expertise that will be helpful to the committee.

Audit Committee

Members are: Kenneth F. Heddon, Chairman; F. Newton Hughes, John E. Poole, Bruce W. Watson and Ardagh S. Kingsmill, secretary.

The responsibilities of this committee have a twofold thrust. One is to assist the Board of Directors in fulfilling its fiduciary responsibility regarding the accounting and reporting practices of the company and ensuring that the financial reporting of the performance of the company to shareholders and others is open and informative. The second is to provide the external and internal auditors of the company with full and direct access to the Board of Directors in order to preserve the auditors' independence in their relationship with management.

Manpower and Board Policy

Members are: Ross A. Hennigar, Chairman; Gordon E. Hillhouse, F. Newton Hughes, Bruce W. Watson and Clifford K. Boland, secretary. Dudley M. McGeer is a member with respect to Board policy only.

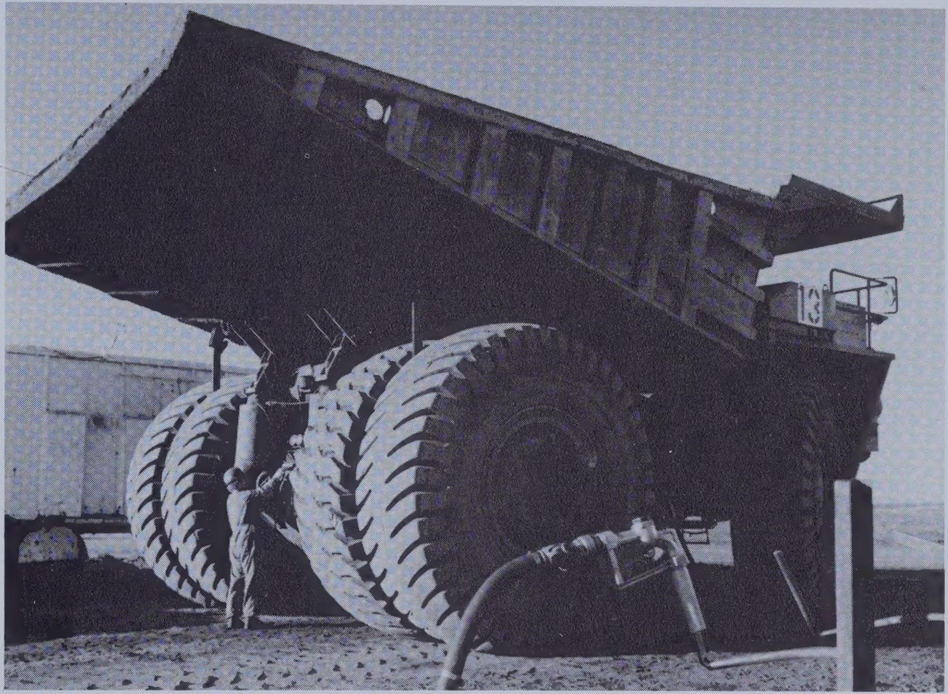
Public Affairs Policy

Members are: Howard B. Maxwell, Chairman; John E. Poole, William S. McGregor and William L. Oliver, secretary.

This committee's role is to assess the company's performance as a corporate citizen and to suggest ways and means by which it can be improved; to ensure that the company's operating practices take the public interest fully into account; to see that company actions are communicated to its various publics; and to apprise the Board of the status of the company's relationship with its publics.

1 Bucketwheel excavator 1340 loads a 150-ton capacity truck with overburden.
2 A giant 150-ton capacity truck stops at "Lube Island" for re-fueling.
3 Cutie O'Riley (left), Geneve Francis, and Geraldine Vardy, cafeteria hostesses, preparing lunch.
4 Store Person, Mel Rewakowsky (left) and a summer student in the Materials Management Yard Warehouse.

1



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3

4

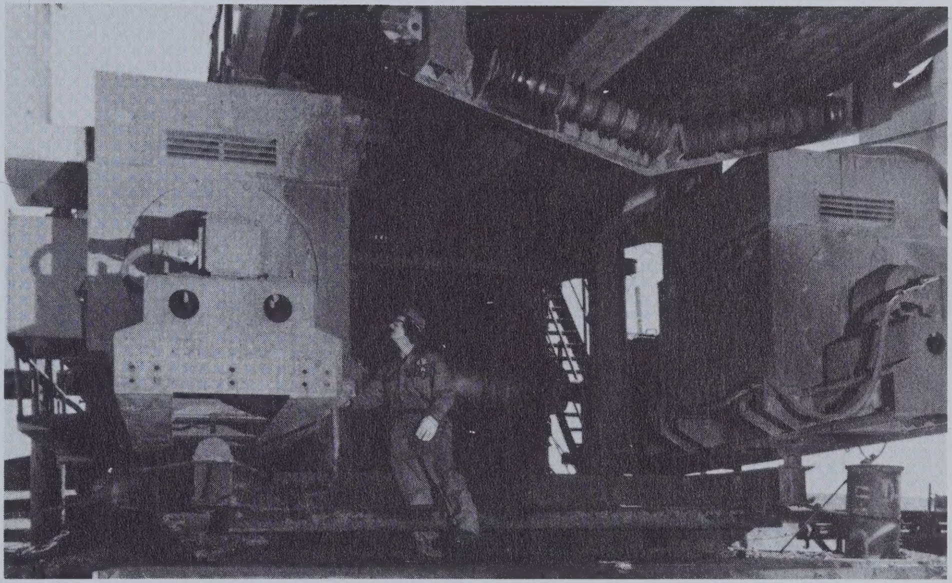
Parent Company
Sun Company, Inc.
Radnor, Pennsylvania

Subsidiary Companies
Athabasca Realty Company Limited
Fort McMurray and Edmonton, Alberta
Employee Housing

Great Canadian Oil Sands Supply Limited
Fort McMurray and Edmonton, Alberta
Provision of materials and supplies

Associated companies in Canada
Sun Oil Company Limited and its subsidiaries
Toronto, Ontario
Integrated petroleum company

Sperry-Sun of Canada Limited
Edmonton, Alberta
Well surveying and engineering services



Employee checks equipment beneath conveyor belt carrying oil sand to extraction plant.

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